THE UNIVERSITY OF ZAMBIA

GRADUATE SCHOOL OF BUSINESS

COURSE NAME: FINANCE FOR MANAGERS.

COURSE CODE: GSB5031

ASSIGNMENT ONE

LECTURER: DR. MARTIN KABWE.

DUE DATE: SEPTEMBER 10, 2023.

TASK:

You are part of management of an investment company wanting to invest in one of the listed companies on Lusaka Securities Exchange. Using the financial statements of any selected listed company (one), write a report analyzing its financial performance and position for the financial year end 2022, and advise whether you should proceed to invest in that company or not. Your report should address the following areas of performance:

i) Profitability
ii) (ii) Liquidity
iii) (iii) Efficiency use of assets
iv) (iv) Leverage
v) (v) Dividend capacity
vi) (vi) Growth prospect

DUE DATE: 10TH SEPTEMBER 2023.

GROUP 10 – MEMBERS:

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INTRODUCTION

As investors contemplating on investing, it is not only vital but a prerequisite to assess the performance and management of the businesses we intend to fund. Some elements investors should consider before investing in any kind of business, include but not limited the financial performance, background and experience in the industry, the uniqueness of a business, market size and business model.

This assignment paper aims to consider the financial performance of a company listed under Lusaka Security Exchange (LUSE), and as group 10, we opted for the Zambia Breweries by using its 2021- 2022 financial for our analysis.

I. PROFITABILITY RATIOS

These ratios measure the efficiency of the activities of a firm and its ability to generate profit. Examples includes, profit (net or gross) margin, return on investment, net profit to network, etc.

2021 (K "000") 2022 (K "000")

A. RETURN ON CAPITAL EMPLOYED

$$ROCE=\frac{Net\,Operating\,Profit}{Employed\,Capital}\times 100\%$$

$$ROCE=\frac{190{,}180}{1{,}662{,}379}\times 100\% \qquad ROCE=\frac{190{,}180}{1{,}686{,}207}$$

X 100%

$$ROCE=\frac{190{,}180}{1{,}662{,}379}\times 100\%$$

$$ROCE=\frac{226{,}989}{1{,}686{,}207}\times 100\%$$

$$ROCE=11.4\% \qquad ROCE=13.5\%$$

$$Capital\,Employed=Total\,Assets-Current\,Liabilites$$

$$CE(2021)=K3{,}578{,}033-K1{,}915{,}654$$

$$CE(2022)=K4{,}672{,}070-K2{,}985{,}863$$

$CE(2021) = K1{,}662{,}\underline{\underline{379}}$ $CE(2022) = K1{,}686{,}207$

B. **OPERATING PROFIT MARGIN**

$$OPM = \frac{Operating\,Profit}{Total\,Revenue} \times 100\%$$

$$OPM = \frac{190{,}180}{3{,}068{,}959} \times 100\% \qquad OPM = \frac{226{,}989}{3{,}601{,}362} \times 100\%$$

$$OPM = \frac{190{,}180}{3{,}068{,}959} \times 100\% \qquad OPM = \frac{226{,}989}{3{,}601{,}362} \times 100\%$$

$$OPM = 6.2\% \qquad \_OPM = 6.3\%$$

C. **GROSS PROFIT MARGIN**

$$Gross\,Profit\,Margin = \frac{Gross\,Profit}{Sales\,revenue} \times 100\%$$

$$¿\frac{1{,}044{,}102}{3{,}068{,}959} \times 100\% \qquad ¿\frac{1{,}342{,}970}{3{,}601{,}362} \times 100\%$$

$$¿\frac{1{,}044{,}102}{3{,}068{,}959} \times 100\% \qquad ¿\frac{1{,}342{,}970}{3{,}601{,}362} \times 100\%$$

$$¿34.02\% \qquad = \underline{\underline{37.29\%}}$$

D. **NET PROFIT MARGIN**

$$Net\,Profit\,Margin = \frac{Net\,Profit}{Total\,Sales} \times 100\%$$

$$NPM = \frac{147{,}952}{3{,}068{,}959} \times 100\% \qquad NPM = \frac{46{,}211}{3{,}601{,}362} \times 100\%$$

$$NPM = 4.82\% \qquad NPM = 1.28\%$$

E. **GROWTH IN SALES**

$$Growth \in Sales = \frac{Prevailing\,Yea\,r'\,s\,Revenue - Former\,Yea\,r'\,sRevenue}{Revenue\,for\,the\,Previous\,Year} \times 100\%$$

$$Growth \in Sales = \frac{3{,}601{,}362 - 3{,}068{,}959}{3{,}068{,}959} \times 100\%$$

$$Growth \in Sales = \frac{532{,}403}{3{,}068{,}959} \times 100\%$$

$$Growth \in Sales = 17.35\%$$

SUMMARY OF THE ANALYSED FINANCIAL RATIOS

RATIOS	2021	2022
RETURN ON CAPITAL EMPLOYED	11.4%	13.5%
OPERATING PROFIT MARGIN	6.2%	6.3%
GROSS PROFIT MARGIN	34.02%	37.29%
NET PROFIT MARGIN	4.82%	1.28%
GROWTH IN SALES		17.35%

A. RETURN ON CAPITAL EMPLOYED

The return on capital employed ratio is a fundamental measure of business performance. This ratio expresses the relationship between the operating profit generated during a period and the average long-term capital invested in the business (Peter Atrill and Eddie McLaney, 2012).

Our analysis pointed out growth in the return on capital employed from 11.4% to 13.5% in the 2021-2022 economic year, which was attributed to the increase in the operating profit from K 190, 180, 000 to K 226, 989, 000 and an increase in capital employed of K 1, 662, 379, 000 in to K 1, 686, 207, 000 in the same period, 2021 to 2022. In effect, this shows that the company performed better in 2022 as it generated a comparatively higher return on the capital employed as compared to the previous financial year.

B. OPERATING PROFIT MARGIN

Peter Atrill and Eddie McLanwy (2016), define operating profit (that is, profit before interest and taxation) is used in this ratio as it represents the profit from trading operations before interest payable is taken into

account. It is normally the most appropriate measure of operational performance, when making comparisons. This is because differences arising from the way in which the business is financed will not influence the measure.

Therefore, a very slight increase (by 0.1%) in the operating profit margin was recorded, from 6.2% in 2021 to 6.3% in 2022. This was because of a sharp increase in other expenses from K 244,307,000 to K 590,794,000 during the period under review.

C. GROSS PROFIT MARGIN

Charles T. Horngren, ET AL., (2014) pose gross profit margin as the ratio relating the gross profit of the business to the sales revenue generated for the same period. Gross profit represents the difference between sales revenue and the cost of sales. The ratio is therefore a measure of profitability in buying (or producing) and selling goods or services before any other expenses are taken into account. As cost of sales represents a major expense for many businesses, a change in this ratio can have a significant effect on the 'bottom line' (that is, the profit for the year.

Our analysis saw the growth in sales revenue in 2022 to K3, 601, 362, 000 from K3,068, 959, 000 in 2021, and Gross Profit rising from K1, 044, 102, 000 to K1, 342, 970, 000 during the same period under review representing 17% and 12% increase respectively.

D. NET PROFIT MARGIN

Profit margin measures how well a company manages its costs per dollar of sales. Zambia Breweries posted an increase in sales of 17.35% that is from K 3,068,959,000 in 2021 to K 3,601,362,000 in 2022. Despite this increase in sales, there was a decrease in the net profit margin from 4.8% to 1.3% which might have resulted from the increase in other expenses and the interest repayment costs.

E. GROWTH IN SALES

While conducting this analysis, there was a 17.35% growth in sales revenue. This increase could be attributed to the additional expenses

which we can assume was on advertisement to create additional demand for the company's commodities.

II. LIQUID RATIO

This is the measure of the ability of a company to fulfil its short-term obligations.

RULE: 2:1

2021 K' 000	**2022 K' 000**
A. $Current\,Ratio=\frac{Current\,Assets}{Current\,Liability}$	
$¿\frac{1,066,702}{1,915,654}$	$¿\frac{1,618,549}{2,985,863}$
$¿0.56$	$¿0.54$

COMMENT: The Zambia Breweries recorded a fall in current ratio from 2 : 0.56 in 2021 to 2 : 0.54 in 2022, which in effect means the company had a higher risk of encountering difficulty meeting its short-term financial obligations.

ACIDITY RATIO

This is aimed at measuring the business's ability to meet its current liabilities should they demand payments simultaneously from its liquid assets.

$$Acid\,Ratio=\frac{Current\,Assets-Inventories}{Current\,Liability}$$

2021 K' 000	**2022 K' 000**
$¿\frac{1,066,702-609,424}{1,915,654}$	$¿\frac{1,618,549-800,697}{2,985,863}$
$¿0.269$ **or (1 : 0.269)**	$¿0.274$ **or (1 : 0.274)**

COMMENT: The ratios presented a very slight increase, though, it portrayed the company's difficulties in funding the current liabilities should the suppliers request for a simultaneous payment bearing in mind the standard 1:1 ratio.

III. EFFICIENCY RATIOS

2021 K'000 **2022 K'000**

a. Settlement period for receivables

¿ $\frac{Total\ Receivables}{Total\ Sales} \times 365\ days$

2021: ¿ $\frac{238{,}316}{3{,}068{,}959} \times 365\ days$ ¿ $28\ days$

2022: ¿ $\frac{423{,}483}{3{,}601{,}362} \times 365\ days$ ¿ $43\ days$

b. Inventory turnover period

¿ $\frac{Average\ Inventories}{Cost\ of\ Goods\ Sold} \times 365\ days$

2021: ¿ $\frac{609{,}424}{2{,}024{,}857} \times 365\ days$ ¿ $110\ days$

2022: ¿ $\frac{800{,}697}{2{,}258{,}392} \times 365\ days$ ¿ $129\ days$

c. Settlement period for payables

¿ $\frac{Total\ Payables}{Cost\ of\ Sales} \times 365\ days$

2021: ¿ $\frac{1{,}218{,}544}{2{,}024{,}857} \times 365\ days$ ¿ $220\ days$

2022: ¿ $\frac{1{,}694{,}190}{2{,}258{,}392} \times 365\ days$ ¿ $274\ days$

SUMMARY

RATIO	2021	2022
Settlement Period - Receivables	28 Days	43 Days
Inventory Turnover Period	110 Days	129 Days
Settlement Period - Payables	220 Days	274 Days

Receivable Period: This shows the number of days Zambia Breweries can take to collect all payments held by customers who might have collected the goods on credit. As a result of this analysis, ZB saw an increase in the number of receivables days to 43 in 2022 against what it had recorded the previous year, 2021. In addition, the levels of receivables also increased to K 423,483 in 2022 from merely K 238,316 in 2021.

Inventory Turnover: Refers to the amount of time that passes from the day an item is purchased by a company until it is sold. One complete

turnover of inventory means the company sold the stock that it purchased, less any items lost to damage or shrinkage.

During the financial years (2021 to 2022), Zambia Breweries saw a sharp increase in the number of inventories held 609,424 to 800,607 and the costs of sales 2,024,857 to 2,258,392 showing its vulnerability in the payable and receivable periods having increased from 110 to 129days.

Payable Period is the measures of the period it takes for a company to pay its creditors for the goods, material, etc gotten on credit, and ZB had experienced an increase in the number of its payable period to 274days against the base year, 2021 having recorded 220 days in that prior year. Trade payables arose from K 1,218,544 in 2021 to K 1,694,190.

IV. LEVERAGE

Leverage ratios are concerned with how much financial leverage the company has taken on. You may wish to know that when a company borrows money, it promises to make a series of interest payments and repay the amount it borrowed. Leverage shows how extensively a company uses debt. It also shows the extent to which the company's asset base is financed by debt.

$$Debt\,Equity\,Ratio=\frac{total\,Liabilities}{Shareholder\,Equity}$$

2021 K'000	2022 K'000

a. $Debt\,Equity\,Ratio=\frac{2,439,029}{1,139,004}$

$Debt\,Equity\,Ratio=\frac{3,486,855}{1,185,215}$

¿2.14 ¿2.49

The debt to equity for ZB rose to from 2.14 in 2021 to 2.94 in 2022. Total liabilities and shareholders' equity simultaneously increased from K 2,439,029 and K 1,139,004 in 2021 to K 3,486,855 and K 1,185,215 in 2022 respectively. An increase in the debt-to-equity ratio translates ZB to have accrued more debts in 2022 as compared to 2021 from the capital market to finance its investments.

$$Interest\,Cover=\frac{Profit\,Before\,Interest \wedge Tax}{Interest\,Payable}$$

2021 K'000	2022 K'000

a. $$Interest\,Cover = \frac{Profit\,Before\,Interest \wedge Tax}{Interest\,Payable}$$

$$Interest\,Cover = \frac{190{,}180}{86{,}936} \qquad Interest\,Cover = \frac{226{,}989}{151{,}839}$$

$$Interest\,Cover = 2.19 \qquad Interest\,Cover = 1.49$$

According to Investopedia, the interest coverage ratio is a debt and profitability ratio used to determine how easily a company can pay interest on its outstanding debt. The interest coverage ratio is calculated by dividing a company's earnings before interest and taxes (EBIT) by its interest expense during a given period. The company in subject, saw a decline interest cover attributable to the rise in financing expenditure from K 86,936 to K 151,839 during the accounting period. This therefore translated to Zambia Breweries having less cash to fund more investments.

V. **DIVIDEND CAPACITY.**

Dividend capacity is the maximum aggregate amount of dividends that a company could declare and pay at such time while maintaining a leverage ratio**.** Conceptually, the company's board, may decide to take the aggregated dividends and declare it as the retained earnings to support further investments therefore inducing the internal growth of the Zambia Breweries.

$$Dividend\,Ratio = \frac{Aggregate\,Dividends}{Net\,Income}$$

2021 K'000	2022 K'000

$$Dividend\,Ratio = \frac{0}{46{,}211} \qquad Dividend\,Ratio = \frac{0}{147{,}952}$$

$$Dividend\,Ratio = 0 \qquad Dividend\,Ratio = 0$$

Comment: The results of the dividend-ratio analysis shows that the company, Zambia Breweries retained all its net income, leaving nothing to be given to shareholders as dividends in the two years under review.

This is attributable to the desire by the board to continue growing the business with the internally sourced funds as compared to the debt financing which might worsen the company's financial situation if that option was considered especially that the debt had grown from K1,915,654 in 2021 to K 2,985,863 in 2022.

$$Dividend\ Yield\ Ratio = \frac{Cash\ Dividend\ Per\ Share}{Prevailing\ Share\ Market\ Value}$$

$$Dividend\ Yield\ Ratio(2021) = \frac{0}{7} \qquad Dividend\ Yield\ Ratio(2022) = \frac{0}{7}$$

$$Dividend\ Yield\ Ratio(2021) = 0 \qquad Dividend\ Yield\ Ratio(2022) = 0$$

VI. GROWTH PROSPECTS.

a. $Price\ Earnings\ Ratio = \frac{Market\ Share\ Value}{Earning\ Per\ Share}$

2021 K'000	2022 K'000
$PER = \frac{7.24}{0.27}$	$PER = \frac{7}{0.08}$
$PER = 26.815$	$PER = 87.5$

b.

$$Price\ earnings ¿\ growth\ ratio = Price ¿\ Earning \frac{¿}{Earning\ Per\ Share\ Growth}$$

2021 Financial Year:

$$Earning\ Per\ Share\ Growth = \frac{EPS2022 - EPS2021}{EPS2021} \times 100\%$$

$$Earning\ Per\ Share\ Growth = \frac{0.08 - 0.27}{0.27} \times 100\%$$

$$Earning\ Per\ Share\ Growth = -70.37\%$$

2022 Financial Year:

$$Earning\ Per\ Share\ Growth = \frac{87.5}{-70.37}$$

$$Earning\ Per\ Share\ Growth = -1.24$$

The P/E ratio is calculated by dividing the market value price per share by the company's earnings per share. A high P/E ratio can mean that a stock's price is high relative to earnings and possibly overvalued. A low P/E ratio might indicate that the current stock price is low relative to earnings.

Despite the challenges faced by Zambia Breweries during the 2021 to 2022 financial year, the company realized an increase in the price-earning ratio to 87.5% in 2022 compared to 26.8 attained the previous year, however, the company had its per share price falling sharply by (70.37%) in 2022, noted from the declared financials representing the 0.08 in 2022 against the 0.27 recorded in 2021.

CONCLUSION

This assignment was aimed at analyzing the audited financial statements thoroughly with regards to the parameters set forth, and therefore, the team opted to looked at the profitability and liquidity, efficiency, leverage / gearing ratios, and dividend and growth capacity of the Zambia Breweries for the 2021/22 economic year and the following was pointed out:

1.

Though Zambia Breweries was hit by the effects of the COVID-19 pandemic during the period under review, recorded several successes in profit parlances, it was noticed that there was:

a. increase in the gross profit margin,
b. a decrease in the net profit margin,
c. slight increase in the operating profit margin,
d. increase in the return on capital employed, and:
e. increase in growth of sales from 2021 to 2022.

Regarding liquidity, the team realized that Zambia Breweries was highly constrained with the capacity to pay liabilities (current) with its most current assets. The efficiency ratios showed that the company

experienced an increase in the inventory turn-over period and settlement period for both receivables and payables.

Moreover, a heavy reliance on debt financing was noticed following the growth in liabilities in 2022, from 697,110 to 1,291,673 adding to the already existing finance troubles facing Zambia Breweries as a company.

Considering the above, it is risky to for would be investors to throw their monetary resources to Zambia Breweries as it may result in prolonged period of no declaration of dividends as noticed from the previous economic years, 2021/22.

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